FILE COPY

Office - Supreme Court, U. S.
FILED
OCT 7 1942
CHARLES ELMORE CROPLEY

IN THE

Supreme Court of the United States

October Term, 1942 **No. 18**

In the Matter of

CHICAGO, MILWAUKEE, ST. PAUL & PACIFIC RAILROAD COMPANY, DEBTOR

GROUP OF INSTITUTIONAL INVESTORS, ET AL.
Petitioners

against

TRUSTEES OF PRINCETON UNIVERSITY, ET AL., constituting the "UNIVERSITY GROUP" of General Mortgage Bondholders of CHICAGO, MILWAUKEE & ST. PAUL RAILWAY COMPANY
Respondents

BRIEF FOR "UNIVERSITY GROUP", RESPONDENTS

FREDERICK J. MOSES
Attorney for Trustees of Princeton University et al., constituting the "University Group" of General Mortgage Bondholders of Chicago, Milwaukee & St. Paul Railway Company
70 Pine Street
New York City

October 7, 1942

TABLE OF CONTENTS.

	PAGE
PRELIMINARY STATEMENT	1
Group Membership	1–2
OPINIONS BELOW	2
STATEMENT	2–8
Petitioners' Contention	2
General Mortgage Lines	4–5
Milwaukee & Northern Mortgage Lines	5
Gary Line	5
"Lines West"	5–6
Terre Haute	6–8
SUMMARY OF ARGUMENT	8–9
ARGUMENT	9–29
I. The law imposes upon the Court full responsibility of determining whether a plan be fair and equitable, etc.	9–12
II. Without a finding that the General Mortgage Lines are not fully secured the Court can not conclude that the Plan is not discriminatory	13–16
III. Determination of what property is subject to each Mortgage, essential	16–19
"Pieces of Lines East"	16–18
IV. There must be findings which will warrant the Court in concluding that the new securities offered are of a value equal to our claims and that full compensatory treatment has been made for the "entire bundle of rights" which we would surrender	19–23

PAGE

Priority 20

"Lines West" 20–21

New securities offered 20–22

Effect of taxation on stocks 22–23

V. There must be findings to warrant the Court in concluding that this Plan, in which junior interests participate, gives due recognition to our superior rights by giving us only a face amount of inferior securities equal to the face amount of our claims 23–24

VI. The provision for Additions and Betterments is unlawful and unnecessary 24–26

VII. There must be findings to warrant the Court in concluding that we should not be subrogated to the rights of the R.F.C. in the collateral for its loan 27–28

VIII. The Commission should be directed to receive evidence of facts and earnings after March, 1938 29

CONCLUSION 29–30

APPENDIX — Exhibit 181 31

TABLE OF AUTHORITIES

	PAGE
FIFTH AMENDMENT TO THE CONSTITUTION	20, 30
Statutes	
Judicial Code, 240a, Sec. 77, Bankruptcy Act (11 U.S.C.A. 205)	
Sec. 77 (b)	10
77 (b) (4)	25
77 (d)	10
77 (e)	3, 10
77 (e) (1)	13
77 (j)	24
Decisions	
Atchison, Topeka & Santa Fe R.R. v. United States, 284 U. S. 248	29
Burgoon v. Lavezzo, 92 Fed. 2nd, 726-36	28
Case v. Los Angeles Lumber Co., 308 U. S. 106	11
Consolidated Rock Products Co. v. DuBois, 312 U. S. 510	3, 4, 11, 12, 16, 19, 21, 23, 24, 30
Investigation of Chicago, Milwaukee & St. Paul Railroad, 131 I. C. C. 615	6
Louisville Bank v. Radford, 295 U. S. 555	20, 21, 29
Merchants & M. Transport Co. v. Robinson & Co., 191 Fed. 769-772	28
Northern Pacific Railway Co. v. Boyd, 228 U. S. 482	11, 12, 24
Palmer v. Massachusetts, 308 U. S. 79, 87	10, 11
Rachal v. Smith, 101 Fed. 159	27
Southwestern Bell Telephone Co. v. Public Service Commission, 262 U. S. 276, 292	26

IN THE

Supreme Court of the United States

October Term, 1942 **No. 18**

In the Matter of

CHICAGO, MILWAUKEE, ST. PAUL & PACIFIC RAILROAD COMPANY, Debtor.

GROUP OF INSTITUTIONAL INVESTORS, *et al.*,
Petitioners,

against

TRUSTEES OF PRINCETON UNIVERSITY, *et al.*, constituting the "UNIVERSITY GROUP" of General Mortgage Bondholders of CHICAGO, MILWAUKEE & ST. PAUL RAILWAY COMPANY,
Respondents.

BRIEF FOR "UNIVERSITY GROUP", RESPONDENTS

These respondents are a group [1] of owners and holders of General Mortgage bonds of the Chicago, Milwaukee & St. Paul Railway Company, the predecessor of the Debtor.

---

[1] This Group was formed to assert and protect the rights of the General Mortgage Bondholders, in the Summer of 1940 when it became apparent that the Institutional and Savings Banks Groups, which had asserted those rights before the Commission, would acquiesce in the Commission's Plan of Reorganization. The members of the Group and their holdings of General Mortgage Bonds are:

The Trustees of Princeton University	$100,000
New York University	25,000
Milbank Memorial Fund	200,000
Bank for Savings of the City of New York	1,100,000
Union Square Savings Bank, New York City	550,000
Greenwich Savings Bank, New York City	179,000

(Continued on next page)

Opinions Below

The reports and orders of the Interstate Commerce Commission are reported at 239 I. C. C. 485 and 240 I. C. C. 257 (Original Report, R. 2153-2269, and Order R. 1258-1283; Supplemental Report, R. 1284-1317, and Supplemental Order, R. 1319-1347). The opinion of the District Court (R. 1857-1899) is in 36 F. (2nd) 193. The opinion of the Circuit Court of Appeals (R. 2297-2317, 2334-35) is in 124 F. (2nd) 754. The *per curiam* opinion of the Circuit Court of Appeals (R. 2234, 5) is not reported.

Statement

Stripped of its verbiage the contention of the petitioners is that the Commission's allocation of new securities under a proposed plan of reorganization constitutes a conclusive finding of the values of the properties subject to the several liens, of the value of each of those liens

Bank of New York, as Trustee	$130,000
New York Trust Company, as Trustee	70,000
U. S. Trust Company of New York, as Trustee for Individual Beneficiaries	481,000
Boston Insurance Company	75,000
Old Colony Insurance Company of Boston	30,000
New Amsterdam Casualty Co. of New York	176,000
First National Bank of Everett, Washington	25,000
Consolidated Investment Trust, Boston	400,000
Robert Winthrop, as Trustee and Guardian	296,000
Edgar Palmer, as Trustee	100,000
E. Sohier Welch and George E. Brown, as Trustees, Boston, Massachusetts	35,000
Grenville L. Winthrop, New York City	110,000
Wood, Struthers & Company, New York City	300,000
Charles M. Wood, Philadelphia, Pa.	247,000
Leo Wallerstein, New York City	50,000
Beekman Winthrop, Individually and as Trustee (now deceased) was a member	273,000

and also a finding that the value of the new securities allocated to each lien equals the value of that lien and of its lost priority.

If this Court decided anything in *Consolidated Rock Products Co.* v. *DuBois*, 312 U. S. 510, it is that such an allocation of securities is not a finding of the value of the liens nor of the new securities allocated, and that without such findings it is impossible for the Court to determine whether the allocation be fair and equitable.

They also assert that it would be "a tremendous task" for the Commission to make a finding of the value of the property subject to each lien and that, therefore, this Court should nullify the express provision of the Statute (Section 77 (e))[2] and the law of the land, declared in the *Consolidated Rock Products* case (312 U. S. 510, p. 526).

It *was* a tremendous task to appraise, for rate-making purposes, the thousands of items of physical property subject to each lien—but that task has been completed and is brought down to date by the Railroad's periodic reports showing additions, retirements and depreciation.

Those values were before the Commission and are stated in its report. Likewise, the earnings of the whole System and an allocation of earnings to the several mortgage divisions (which the Commission accepted as evidence of earning capacity and made the "basis" of its report (R. 2251)) and "all other relevant facts" were before the Commission.

---

[2] "If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts."

Having before it all of the factors required as the basis of its valuation, the Commission had only to exercise its sound judgment as to the "approximate value" of each mortgage division (*Consolidated Rock Products Co.* v. *DuBois*, 312 U. S. 510, p. 525), whether it be greater or less than the lien, and if the lien be not fully secured by how much or by what percentage the security fails to equal the amount of the lien.

The General Mortgage Lines

The General Mortgage made by the predecessor of the Debtor in 1899 (securing $150,000,000, of which $138,788,000 bonds are outstanding in the hands of the public (R. 2269)) is a first lien on some 6,000 miles of railroad, of which the elements of physical value were appraised for rate-making purposes by the Commission at about $359,000,000 (R. 2215).

The Commission's report states that the earnings of the General Mortgage Lines for 1936 were $8,716,847 (R. 2250), at the rate of almost exactly 2⅓% of the physical value of the property. It was proved before the District Court, that during the first three and one-half years of operation by the Trustees in Bankruptcy, from July 1, 1935 to December 31, 1938, the General Mortgage Lines earned $26,817,802, about the same rate (R. 220) or about $6,000,000 more than the bond interest accrued during that period.

The General Mortgage is also a first lien on rolling stock worth, after depreciation, about $49,000,000 over and above equipment liens on a part thereof as of June 30, 1935.

The allocation of earnings of the several mortgage divisions (Ex. 181, R. 723)[3] was accepted by the Commis-

[3] None of the exhibits is printed in the record. The references are to the pages at which they were put in evidence.

For the convenience of the Court we have printed a copy of Exhibit 181 as an appendix to this brief.

sion as evidence of earning power and made the "basis" of its Plan (R. 2251). It shows that after deducting from the earnings of the General Mortgage Lines the total sum credited to the Terre Haute for hauling Company coal for the Milwaukee System (about $1,250,000), and over $1,100,000 for interest on equipment obligations, those Lines earned 1.16 times the interest on the entire $150,000,000 of General Mortgage bonds, including $560,600 interest on $11,212,000 owned by the Milwaukee and pledged as security for the loan of the R. F. C. (Ex. 181, Footnote (d), R. 723), and about 1.27 times the interest on the bonds held by the public.

The Milwaukee & Northern Mortgage Lines

The Milwaukee & Northern and the General Mortgage Lines were the only Lines which were operated at a profit (Ex. 181, R. 723).

It was proved before the District Court that the Milwaukee and Northern Consolidated Lines have become permanently deficit lines (Court Exs. 28, 29, 30; R. 1723, and R. 1746-8).

The Gary Line

The Gary is a deficit line (Ex. 181; R. 723).

The "Lines West"

Regarding the "Lines West" (some 2,860 miles of railroad extending from the Missouri River to the Pacific Coast), the Commission reported:

> "We are satisfied that on any reasonable basis of allocation between the Lines West and the other parts of the System, the Lines West cannot be expected to earn any sum for the payment of interest." (R. 1307-8).

This finding is confirmed by proof before the District Court that during the first 3½ years of operation by the Trustees in Bankruptcy, the "Lines West" had an operating deficit of $5,392,544 (R. 1780-81).

The Terre Haute

In 1921, the Milwaukee bought 97% of the stock of the Terre Haute (which it still owns) at $10 per share and made a lease for 999 years by which (among other things) it guaranteed the principal and interest of about $22,000,000 of Terre Haute bonds—at the rate of about $65,000 per mile on the 320 miles of Terre Haute road, valued by the Commission at about $1,000,000 less than the mortgage debt. (The General Mortgage is at the rate of about $25,000 per mile on the 6,000 miles of General Mortgage Lines.)

The Plan contemplates that 120 miles from Latta to Westport (Court Ex. 15, R. 1685, and Ex. 77, R. 300), one-third of the Terre Haute mileage, shall be abandoned (R. 2236); which will make the Terre Haute mortgage liens more than $90,000 per mile.

The Plan awards to the General Mortgage bondholders, new First Mortgage bonds at the rate of about $6,500 per mile of their lines.

The Commission in its Supplemental Report stated (R. 1304):

> "* * * we consider that *there is no justification* for the approval of a plan based upon the assumption by the new company of the lease, the guaranty of the Terre Haute income bonds and the other obligations growing out of the lease." (Italics ours.)

The Court below said of the Terre Haute (R. 2305):

> "* * * the report of the I. C. C.[4] upon the value of these bonds and the circumstances under which the

[4] (This refers to *Investigation of* CHICAGO, MILWAUKEE & ST. PAUL RAILROAD, 131 I. C. C. 615.)

road was acquired, have given this transaction a malodorous reputation."

And, again (R. 2311, Footnote):

"* * * A management with ethics which would tolerate the Terre Haute transaction were sure, sooner or later, to be applying to a court of equity or court of bankruptcy for protection against the hordes of insistent claimants with past due unpaid obligations."

The Terre Haute Corporation, and the several classes of Terre Haute bondholders have an *unsecured* contract claim against the *bankrupt* Debtor; and the Plan provides that if the lease be disaffirmed they shall prove their unsecured claim and receive the same treatment as other unsecured creditors (R. 1306).

Nevertheless, the Plan offers these unsecured creditors a guaranty, by the *solvent* reorganized Milwaukee, of the principal of their bonds, of 2¾% in fixed interest and 1½% contingent interest thereon. This would give them $600,000 (R. 1303) of the income available for fixed charges, or about 40% as much as is allotted to the underlying General Mortgage. And, for good measure, the Plan increases from 4% to 4¼% the interest on one-third of the Terre Haute bonds (the Indiana Southern 4s) which have a first lien on the one-third of the road which is to be abandoned.

Before the District Court it was proved that year by year from 1925; the quantities of both commercial and Milwaukee coal hauled over the Terre Haute decreased until in 1937 each was less than two-thirds of the quantity hauled in 1925 (Court Ex. 23, R. 1688 and R. 1707). There was also evidence of some of the amazing economy and efficiency resulting from the introduction of the Diesel locomotive (R. 1513-17).

Mr. Scandrett, one of the Trustees in Bankruptcy, testified that if the lease were disaffirmed, the Milwaukee

could purchase coal at the Indiana mines, ship it over the Terre Haute, that any profit to the Terre Haute would ultimately go to the Milwaukee as owner of 97% of the Terre Haute stock, and that if (instead of a new lease) an operating agreement were made the Milwaukee would not have to meet the maturity of the Terre Haute bonds (R. 1522-3).

The Court below said (R. 2314):

> "It is impossible to approve the disposition of the Terre Haute bond issues without more specific findings. Whether this lease should not be now terminated presents a separate question which can only be determined when findings are made."

Summary of Argument

I. The law imposes on the Court the full responsibility and the duty to determine whether or not the Plan, certified by the Commission to be "compatible with the public interest", be in conformity with the requirements of the law.

II. Without findings of value the Court cannot determine whether or not the Plan discriminates unfairly in favor of any class of creditors.

III. Without a determination of what property is subject to each mortgage, the Court cannot determine whether or not the Plan be fair and equitable.

IV. There must be findings upon which the Court can determine whether or not the new securities offered are of a value equal to our claims and that we receive full compensatory treatment for the entire bundle of rights which we would surrender.

V. Without a finding that the new securities offered are not inferior to the present General Mortgage bonds,

the Court cannot conclude that this Plan, which offers to these bondholders a face amount of "new securities equal to the face amount of their claims" and "nothing in addition (as) compensation for their senior rights which they are to surrender", is fair and equitable and in conformity with the requirements of the law.

VI. The provision for the Additions and Betterments Fund is unlawful and unnecessary.

VII. There must be findings to warrant the Court in concluding that the creditors to whom New First Mortgage bonds are awarded, should not be subrogated to the rights of the Reconstruction Finance Corporation in the securities held as collateral for its loan.

VIII. The Commission should be directed to receive evidence of facts and earnings after the date when its hearings closed in March, 1938, and to consider such evidence as well as the evidence received in the District Court.

POINT I

The law imposes upon the Court the full responsibility of determining whether or not a plan of reorganization be fair and equitable and in conformity with the requirements of the law.

The petitioners' whole argument is based on what we believe to be an erroneous assumption of the law, that the report and the Plan certified to the Court by the Interstate Commerce Commission have the same status before the Court as the Commission's reports and orders in rate cases where it has original and exclusive jurisdiction, and which the Courts will not nullify if there be any evidence to support the Commission's order.

As this Court said in *Palmer* v. *Massachusetts*, 308 U. S. 79, 87 (1939), at the time of the enactment of Section 77 in 1933,

> "There was a strong sentiment in Congress to withdraw from the courts control over insolvent railroads and lodge it with the Interstate Commerce Commission. Congress stopped short of this remedy."

So, it was not by inadvertence that the Act provides (Section 77(d)) that the Commission shall certify to the Court a plan of reorganization that will, "in its opinion, meet with the requirements of Sub-sections (b) and (e) of this Section and will be compatible with the public interest"; and further provides (Section 77(e)) that "the judge shall approve the plan if satisfied that it complies with the provisions of Sub-section (b) of this Section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders"; and further (Section 77(e)), "If the judge shall not approve the plan • • • he may either dismiss the proceedings or, in his discretion, • • • refer the proceedings back to the Commission for further action."

These last provisions place upon the Court the full responsibility of determining whether or not the Plan be in conformity with those requirements.

The Statute contemplates that there may be railroads as to which no plan can be formulated which will conform with the requirements of the law.

It is the function of the Commission to protect the interests of the public; it is equally the function of the Court to protect the interests of citizens.

The Court below was correct in holding that it is not a "rubber stamp" for the Commission and in refusing to shirk its responsibility. It said in this case (R. 2315):

"• • • *Likewise, the findings must be so specific that the court may definitely see that in the new plan, provision for full compensation of cancelled old senior securities, and all prior preferred positions, is made.* The findings must be sufficiently complete on these matters, that the court may, from its examination, ascertain whether full compensation has been made for the entire bundle of rights which each of the creditors is called upon to surrender.

"It would be begging the question to assume that findings were necessarily made by the I. C. C. when the allocation was made. We would be delegating to the I. C. C. an obligation which is ours. The Commission must formulate its plan. It must make fact findings supported by the evidence upon which its plan is based. We must independently determine whether the plan is fair and equitable. In reaching our conclusion we must ascertain (a) whether there is evidence sufficient to support the findings and (b) we must be able to say that the findings support the plan, and (c) the plan is fair and equitable." (Italics the Court's.)

To hold otherwise would be to delegate to the Commission complete control over reorganizations and vest in it the power to deprive the citizen of his property without due process of law.

The Constitution vests the entire judicial power of the United States in the Supreme Court and such inferior courts as may be created by the Congress. The Congress cannot, and the language above quoted from the opinion in *Palmer* v. *Massachusetts*, 308 U. S. 79, 87 (1939), shows it did not intend to confer judicial power on an administrative body although there was a "strong sentiment" in favor of doing so.

The "full and absolute priority rule of *Northern Pacific R.R. Co.* v. *Boyd*, 228 U. S. 482" was established in the case of a railroad reorganization. In *Case* v. *Los Angeles Lumber Co.*, 308 U. S. 106, and *Consolidated Rock Products Co.* v. *DuBois*, 312 U. S. 510, this Court reit-

erated and emphasized the "full and absolute priority rule" of the *Boyd* case and held that it applies also to the reorganization of commercial corporations.

In the *Consolidated Rock Products* case (312 U. S. 510), the District Court found it impossible to determine what property was subject to the several mortgage liens and that it was likewise impossible to determine the value of the respective properties. This Court held that despite the difficulties some formula must be found which would at least approximately fix the values. In that case, as in the case at bar, there was an allocation of securities to several lienors, and it was argued there, as it is here, that that allocation constituted a finding of the values of the respective properties. This Court held that without findings of the value of the properties subject to the several liens, it "was in no position to exercise the 'informed, independent judgment' which appraisal of the fairness of a plan of reorganization entails" (312 U. S. 510, p. 520), and that it could not determine whether or not that allocation of securities were fair and equitable—whether or not senior lienors would receive compensation for their "entire bundle of rights".

The petitioners now ask this Court to send the case back to the Circuit Court of Appeals and direct that Court to do something which both Courts have declared to be impossible.

POINT II

A Plan which treats one class of fully secured creditors less favorably than other fully secured or unsecured creditors is discriminatory and unlawful, and, without a finding that the General Mortgage is not fully secured, the Court could not conclude that the Plan is not discriminatory.

The Statute, Section 77(e)(1), provides that the Court must be satisfied that the Plan does not "discriminate unfairly in favor of any class of creditors".

It is axiomatic that no creditor, however great be the security for his claim, is entitled to more than payment in full. It is a fundamental principle of the Bankruptcy Law that no fully secured creditor can be deprived of his security without satisfaction of his claim.

The claim of the Reconstruction Finance Corporation for about $12,000,000 is fully secured by collateral. The Plan awards to the R. F. C. 100% of its claim in new First Mortgage Fixed Interest bonds. The Milwaukee & Northern First Mortgage bonds, aggregating $2,117,000, are fully secured by property valued for rate-making purposes at over $4,200,000, earning more than the bond interest (R. 2248). The Plan allots to them 70% of their claim in new First Mortgage Fixed Interest bonds and 30% in Second Mortgage Contingent Interest Series A bonds.

The General Mortgage, made in 1889, is secured by a first lien on about 6,000 miles of railroad, which the Commission describes as the "Heart of the System", including terminals, shops for the building and repair of cars and locomotives, and everything that goes to make up a complete railroad system, having physical elements of value of about $359,000,000 (R. 2215, 2250; I. C. C. Bureau of Valuation Report, Sheet 4). This does not include the

"Pieces of Lines East". It is a lien on locomotives, cars and other equipment, the equity in which is valued at about $49,000,000. This Mortgage secures $150,000,000 bonds, of which about $139,000,000 are outstanding in the hands of the public, the balance being owned by the Company and pledged as security for the claim of the Reconstruction Finance Corporation.

For nearly fifty years the interest on the General Mortgage bonds was paid regularly until this proceeding was commenced in June, 1935. Their annual interest amounts to a little less than $6,000,000. The Report states that in 1936 the income available for interest of the General Mortgage Lines was over $8,700,000 (or 2⅓% of the Commission's valuation of the physical property), and after deducting interest on equipment obligations, more than $7,500,000 (R. 2250); 1.16 times the interest on all the bonds, including those pledged with the R. F. C., and about 1.27 times the interest on the bonds in the hands of the public (Ex. 181, R. 723).

The record shows that during the first 3½ years of operation by the Trustees in Bankruptcy, ending December 31, 1938, the General Mortgage Lines (not including the Pieces of Lines East (R. 231)), earned for interest more than $26,800,000—about $6,000,000 more than the bond interest (R. 229).

The Earnings Studies, which were made the "basis" (R. 2251) of the Commission's Report (assembled in Exhibit 181 (R. 723)), show that the General Mortgage Lines earned more than 88 per cent. of the income available for fixed charges of the System and that with the exception of the Milwaukee & Northern they were the only Lines owned by the Milwaukee operated at a profit.

The finding of the Commission that the probable future earnings available for the payment of fixed charges of the Milwaukee System—$7,859,106—represents the Commission's estimate of what will be left of the earnings of the General Mortgage Lines after paying therefrom the

deficits of the unprofitable lines. The Plan allots to the General Mortgage Lines $1,563,682 (less than one-fifth of that $7,859,106) as interest on new First Mortgage bonds (R. 1317)..

The earnings for 1939 and 1940 were larger than those of the preceding years.

There has been no finding, and we claim that there is no basis for a finding, that the General Mortgage bonds are not fully secured. Nevertheless, the Plan, which allots to other fully secured creditors 100% and 70% of their claims in New First Mortgage Fixed Interest bonds, allots to the General Mortgage bondholders only 25% of their claim in new First Mortgage bonds; 35% in Series A Second Mortgage Income bonds; 20% in Series B Second Mortgage Income bonds and 20% in Preferred Stock.

The Circuit Court of Appeals in its opinion said that there were huge sums of interest unpaid on the General Mortgage bonds. That unpaid interest has all accrued since the property was placed in the hands of the Trustees in Bankruptcy. These huge sums were unpaid when the case was before the Circuit Court of Appeals, not because they were not earned but because the money was used for other purposes and accumulated in the hands of the Trustees in Bankruptcy.

Unless there be a finding that the General Mortgage is not fully secured and that the property subject to its lien is worth much less than the mortgage debt, the Court cannot conclude that these three allocations of securities do not discriminate unfairly in favor of the R. F. C. and the Northern bondholders.

The Plan not only allots to the Terre Haute bondholders, *unsecured* creditors of the Milwaukee, $603,000 in fixed interest (nearly 40% as much as the $1,564,000 allotted to the General Mortgage), giving them priority over 75% of the claim of the Generals, and about $329,000 in contingent interest which would have priority over 40% of the claim of the Generals (all of which should go

to the Generals), but also leaves their lien undisturbed and the new solvent Milwaukee guarantees the payment of the principal.

The Court below held that it could not approve this provision of the Plan without findings to support it.

The petitioners say that they do not know what findings should be made to support it. We know of nothing in or out of the record that would support a finding or a conclusion that it is not unfair discrimination to give to these unsecured creditors priority over the first mortgage creditors.

POINT III

A determination of what property is subject to the respective mortgages is essential and without such a determination the Court could not approve the Plan.

This Court said in the *Consolidated Rock Products* case (312 U. S. 510, p. 520):

> "In the first place there must be a determination of what assets are subject to the payment of the respective claims. This obvious requirement was not met."

And again (p. 524):

> "There is another reason why the failure to ascertain what assets are subject to the payment of the Union and Consumers bonds is fatal. There is a question of the fairness of the plan as respects the bondholders *inter sese.*"

If there be a word more emphatic than "fatal" it is not in our vocabulary.

The "Pieces of Lines East" are 17 short lines, east of the Missouri River, aggregating 574.94 miles (R. 221-2); all branches, cut-offs or connections between points

on the General Mortgage Lines. One (from Bowdle to Mobridge (R. 222)) connects the General Mortgage Lines with the "Lines West".

The General Mortgage, made in 1889, contains an after-acquired property clause and a covenant for further assurances (quoted in Footnote below [5]). (Ex. 23, R. 278).

The 50-Year Mortgage, made in 1928, describes all of the property then owned by the Milwaukee, including these

---

[5] NOW, THEREFORE, THIS INDENTURE WITNESSETH: THAT the party of the first part * * * to secure the payment * * * of said bonds * * * has granted * * * to the UNITED STATES TRUST COMPANY OF NEW YORK * * * as Trustee * * * all and singular the railway and railways of said party of the first part, with the roadbeds, grades, rights-of-way, bridges, depot grounds and fixtures embracing and including all its franchises and privileges appertaining to said railways, now held by said (Railway) Company, amounting in the aggregate to about 5,652 miles of railway in actual operation, described as follows:"

(Here follows a description of railroad property and equipment.)

From page 14 of the General Mortgage:

"TOGETHER with all and singular the rights, privileges and corporate franchises connected with or relating to said railways, or to the construction, maintenance, use and operation of the same, *whether now owned or constructed, or hereafter to be acquired or constructed* * * * and also all the estate, right, title, interest, property, claim, possession and demand whatsoever as well in law as in equity of the said party of the first part, which it now has or may hereafter acquire, of, in and to the same and every part thereof * * *." (Italics ours.)

From pages 35 and 36 of the General Mortgage:

"ARTICLE XX. The said party of the first part * * * hereby covenants * * * to execute and deliver any other and reasonable and necessary deed or deeds, conveyance, or conveyances * * * for the more fully securing the payment of said bonds, *particularly for the conveyance of any railways, lots, blocks, lands, property or premises, or any right or interest therein acquired by said party of the first part,* or its successor, or successors, *subsequent to the date hereof pertaining to the premises conveyed by this Indenture, whether now owned by the party of the first part, or hereafter acquired.*" (Italics ours.)

"Pieces of Lines East", but the *habendum* clause contains the following proviso (Ex. 27, pp. 49-50, R. 280):

> "SUBJECT, HOWEVER, in so far * * * as in law the the same * * * may attach, * * * to existing liens * * * of record * * * and specifically, * * * to the following mortgages * * *
>
> "(c) the General Mortgage, dated May 1, 1889 * * *".

The First & Refunding Mortgage contains the same provision (Ex. 25, pp. 41-42, R. 279).

The Commission expressly declined to pass on the question whether these "Pieces of Lines East" are or are not subject to the General Mortgage (R. 1151).

The earnings of these "Pieces of Lines East" were credited to the 50-Year Mortgage Lines and not to the General Mortgage before the Interstate Commerce Commission (Ex. 181) and before the District Court (R. 224).

The Commission in its Report said (R. 2252):

> "The propriety of crediting the First and Refunding Mortgage, or the 50-Year Mortgage with the earnings of the 'Pieces of Lines East' is rendered doubtful in the absence of a judicial determination of the question whether these lines are subject to the first lien of the First and Refunding Mortgage or to that of the General Mortgage."

This question was raised in both Courts below by "Objections to the Plan" and "Grounds of Appeal", but it was not decided.

The petitioners ask the Court to apply the maxim *de minimis non curat lex* and to disregard this question.

The mileage of these "Pieces of Lines East" is nearly five times that of the Northern 1st Mortgage Lines, more than twice that of the Northern Consolidated Lines, nearly seven times that of the Gary, and more than twice what will be left of the Terre Haute when the line from Latta

to Westport shall have been abandoned (as recommended in the Commission's report), and more than ⅓th that of the great transcontinental "Lines West".

Exhibit 181 shows that in 1936 their Total Commercial Revenue (*i. e.*, Gross Operating Revenue) was $4,596,200—more than one-quarter as much as the "Lines West": $1,300,000 more than the combined Northern Lines; about 25 times that of the Gary and only $700,000 less than those of the Terre Haute; that their "Net Revenue from Railway Operation" was $1,456,800—only $600,000 less than the Terre Haute; $300,000 more than the Northern and 70 per cent. as much as the 2,860 miles of "Lines West".

In 1936 they earned net $170,100 as against a deficit of $1,108,535 for the "Lines West" (Ex. 181) and for the 3½ years (July 1, 1935 to December 31, 1938) $691,678 (Ct. Ex. 34, p. 2, Line 46; R. 1781) as against a deficit of $6,000,000 for the "Lines West" (R. 1783).

How can it be said that this property is negligible?

POINT IV

There must be findings which will warrant the Court in concluding that the "new securities offered are of a value equal to" our claims and that "full compensatory treatment" has been "made for the entire bundle of rights" which we would surrender.

This Court held in the *Consolidated Rock Products* case (312 U. S. 510, 515) that divisional mortgages may be eliminated and a simplified capital structure substituted, but declared as a condition precedent that the new securities offered be of a value equal to the creditors' claims, and held also that the bondholders must receive full compensatory treatment for the "entire bundle of rights" which they surrender.

Not only must there be a finding of the value of our claims but there must be findings upon which the Court can conclude that the plan fulfills those conditions.

Priority

We have now a first lien, prior to all the world including the public interest, on nearly all of the valuable property owned by the Debtor.

In *Louisville National Bank* v. *Radford*, 295 U. S. 555, 602, this Court, holding the Frazier-Lemke Act unconstitutional, said:

> "For the Fifth Amendment commands that, however great the Nation's need, private property shall not be thus taken even for a wholly public use without just compensation. If the public interest requires, and permits, the taking of property of individual mortgagees in order to relieve the necessities of individual mortgagors, resort must be had to proceedings by eminent domain; so that, through taxation, the burden of the relief afforded in the public interest may be borne by the public."

We are offered 25% of our claim in new Fixed Interest 4% bonds (nearly $82,000,000 General Mortgage bonds bear interest at from 4¼% to 4¾%—less than $9,000,000 at a rate lower than 4%) secured by a First Mortgage not on the valuable General Mortgage Lines but on the whole System, *including the deficit lines.*[6]

---

[6] The General Mortgage Lines upon which we have a prior lien have a value far beyond the amount of our Mortgage. They constitute a complete railway system which has always operated at a profit over its bond interest.

The bankruptcy of the Milwaukee resulted from taking General Mortgage earnings to pay operating deficits of the "Lines West" and interest on nearly $300,000,000 bonds which are liens thereon. The Commission has found that those lines cannot be expected to earn anything for the payment of interest.

As this Court has established the law that earning capacity is the sole criterion of value—no commercial value can be attributed to them. The only justification for their continued operation is to render service to the public. But, if the public interest require their

There must be a finding, or findings, from which this Court can conclude that these new First Mortgage bonds offered us are of a value equal to 25% of our claim.

The remaining 75% of our claim is subordinated to the other First Mortgage bonds to be issued, to 2¾% interest on about $22,000,000 of Terre Haute bonds, to $2,500,000 to be used annually for capital expenditures and also income and excess profits taxes thereon. It may also be subordinated to untold millions of new First Mortgage bonds to be hereafter issued, for this Mortgage is to be unlimited in amount (R. 2227).

For the next 35% of our claim we are offered Series A Second Mortgage Income bonds upon which interest can be paid only after the annual payments above described.

There must be findings to warrant the Court in concluding that those bonds are of a value equal to 35% of our claim.

For the next 20% of our claim, we are offered Series B Second Mortgage Income bonds upon which interest can be paid only after interest on the Series A bonds, 1½% on the Terre Haute bonds, and, in the discretion of the directors, after another $2,500,000 plus 4% of all revenue in excess of $100,000,000 in any year, for capital expenditures, and also income and excess profits taxes thereon.

---

continued operation it should be done at public expense. (*Louisville Bank* v. *Radford*, 295 U. S. 555, p. 602).

The reason that the Commission's estimate of probable future earnings is so small is because the operating deficits of the "Lines West" must first be deducted from the earnings of the General Mortgage Lines, and the Plan proposes to saddle upon those earnings, not only the operating deficits but also the cost of additions and betterments to the "Lines West".

In order to accomplish this public benefaction, our priority and our lien are destroyed; we are offered progressively inferior engravings which cannot be dignified with the name "securities".

This does not "afford due recognition to our rights"; it does not "conform to the requirements of the law of the land", established by the Fifth Amendment to the Constitution and the decisions of this Court in *Louisville Bank* v. *Radford*, 295 U. S. 555, p. 602 and *Consolidated Rock Products Co.* v. *DuBois*, 312 U. S. 510.

There must be findings which would warrant the Court in concluding that these Class B bonds are of a value equal to the next 20% of our claim.

Then we are offered 20% of our claim in Preferred Stock, which can receive dividends only after all of the foregoing shall have been paid, and also income and excess profits taxes on any income remaining for such dividends.

The Commission held that the old preferred stock is worthless because the Company must earn about $21,000,000 before it could receive anything and about $28,000,000 before it could receive its full dividends.

It has been computed that under the 1941 Revenue Act, of which this Court will take judicial notice, the reorganized Company would have to earn over $10,700,000 to pay the Class A interest, over $21,000,000 to pay the Class B interest, and nearly $44,000,000 to pay the Preferred Stock dividends—many times what the Commission estimated to be the probable future earnings, and $11,000,000 more than the Milwaukee earned in its most prosperous year (R. 2180). The earnings would have to reach astronomical figures to pay the $3.50 dividends contemplated by the Plan (R. 2242) on the $215,000,000 Common Stock. The Milwaukee never earned as much as $33,000,000.

There must be findings that would warrant the Court in concluding that this new preferred stock is of a value equal to 20% of our claim.

The avowed purpose of reducing the bonded indebtedness to such a low figure is to make sure that the reorganized company can carry on in periods of possible low earnings. Income bonds, contingent on earnings, with voting rights would be just as effective for that purpose and if the Company continue to prosper those who loaned their money would get returns on their investment. It is not "compatible with the public interest" to so arrange the new capitalization that those returns will go instead

to the Government in taxes, because it is unfair, inequitable and confiscatory. Confiscation is never "compatible with the public interest", except as a penalty for wrongdoing.

POINT V

There must be findings as to the value of the new securities offered to warrant the Court in concluding that this Plan, in which junior interests participate, gives due recognition to our superior rights by giving us only a face amount of inferior securities equal to the face amount of our claim.

In the *Consolidated Rock Products* case (312 U. S. 510, 528-9) this Court said:

> "* * * Thus it is plain that while creditors may be given inferior grades of securities, their 'superior rights' must be recognized. Clearly, those prior rights are not recognized, in cases where stockholders are participating in the plan, if creditors are given only a face amount of inferior securities equal to the face amount of their claims. They must receive, in addition, compensation for the senior rights which they are to surrender. If they receive less than that full compensatory treatment, some of their property rights will be appropriated for the benefit of stockholders without compensation. That is not permissible."

The same opinion stated that "Unless meticulous regard for earning capacity be had, indefensible participation of *junior securities* in plans of reorganization may result" (312 U. S. 510, pp. 525-6). (Italics ours.)

So we feel justified in asserting that this Court intended the rule to apply as between senior and junior creditors as well as between creditors and stockholders.

The Commission expressly refused to give the General Mortgage bondholders as compensation for their senior

rights anything more than the face of their claim in inferior securities (R. 2255).

This Court further said in the *Consolidated Rock Products* case (312 U. S. 510, 529):

> "* * * As indicated in the *Boyd* case (228 U. S. at p. 508) the creditors are entitled to have the full value of the property, whether 'present or prospective, for dividends or only for purposes of control', first appropriated to payment of their claims."

The control of the reorganized Company is given to the lowest grade of creditors who receive the common stock which cannot conceivably have any value except its voting rights.

The only thing of value which could be given to senior lienors as even partial compensation for the loss of their senior rights would be to place the voting control of the new Company in holders of new bonds.

POINT VI

The provision for the Additions and Betterments Fund is unlawful and unnecessary.

We have a first lien on physical property valued at more than 2½ times the face of our Mortgage. The Commission has found that the probable future earnings of that property, after deducting the deficits of other lines, amounting to more than $1,000,000 a year, and after paying $1,100,000 interest on equipment obligations, which are undisturbable under the Statute,[1] amount to about $7,500,000

[1] (Sec. 77(j)) "* * * The title of any owner, whether as trustee or otherwise, to rolling-stock equipment leased or conditionally sold to the debtor, and any right of such owner to take possession of such property in compliance with the provisions of any such lease or conditional sale contract, shall not be affected by the provisions of this section."

per year. The interest on our Mortgage amounts to about $6,000,000.

Our present right is to have our principal secured by this property and have its earnings applied, so far as may be necessary, to the payment of our interest. The Commission has deducted a little over $1,000,000 as a factor of safety (as coverage in case its estimate be too high), leaving over $6,500,000 available for fixed charges.

Instead of applying that amount, as far as necessary, to the payment of General Mortgage interest the Commission first deducts $2,500,000 to be used for capital expenditures—additions and betterments—not to the 6,000 miles of General Mortgage Lines but to the whole 11,000 miles of road owned by the System.

We contend, as did the petitioners before the Interstate Commerce Commission, that the provision of Section 77(b)(4)[8] contemplates that the probable future earnings found to be available for fixed charges shall be used in payment thereof and that this Statute, being in derogation of the common law, no power not expressly conferred upon the Commission can be inferred or deemed to be implied. This provision not only reduces by $62,500,000 the fixed interest bonds otherwise available for distribution under the Plan, but during the fifty-year life of the New First Mortgage diverts $125,000,000 (which should go to us as interest) to capital expenditures for the benefit of junior creditors who would become stockholders under the Plan.

The need for a strict construction of the grant of power is emphasized by the fact that we have here the anomalous

---

[8] A plan of reorganization "* * * (4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such amount that, after due consideration of the probable prospective earnings of the property in light of its earnings, experience, and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof;".

position of the body which fixes the rates upon which railroad earnings depend, also clothed with authority to cut down the railroads' capitalization to fit the rates which it had previously made—wiping out in this instance hundreds of millions and in the aggregate of all reorganized railroads, billions of actual invested capital. Having done that they may again reduce the rates to fit the new capitalization and so *ad infinitum*, or rather *ad infinitessimum*.

This is the vicious circle condemned by Mr. Justice BRANDEIS in *Southwestern Bell Telephone Co.* v. *Public Service Commission*, 262 U. S. 276, p. 292.

But even if the Statute conferred upon the Commission power to divert available earnings to capital expenditures, it could not be done without giving us compensation for our lost priority right.

Moreover this provision for Additions and Betterments is unnecessary. Upon a property which the Commission capitalizes at $548,533,321 (R. 2219) it provides for a first mortgage, unlimited in amount, and for the present issuance of First Mortgage bonds of less than $59,000,000—less than 11% of the capitalization. The Plan provides for new bonds to be issued to provide for or to reimburse the new company for not exceeding 75% of such expenditures not including Additions and Betterments to equipment (R. 2228). Why should the bond issue be so small and why should the Mortgage be unlimited in amount except to provide for Additions and Betterments?

Capital expenditures should be made from surplus earnings, or from new capital, and this Plan provides a reservoir of new capital upon which the Company may draw, if necessary, in any year when there are no surplus earnings.

POINT VII

There must be findings to warrant the Court in concluding that the creditors to whom New First Mortgage bonds are awarded should not be subrogated to the rights of the Reconstruction Finance Corporation in the securities held as collateral for its loan.

The claim of the Reconstruction Finance Corporation of about $12,000,000 is secured by Series G General Mortgage bonds, by the 1st and Refunding Mortgage bonds and by other collateral.

The Plan provides that instead of permitting the Reconstruction Finance Corporation to realize on its collateral, the loan shall be paid 100% in New First Mortgage bonds.

This reduces by about $12,000,000 the First Mortgage bonds which would be distributable to General and Milwaukee & Northern bondholders.

For all practical purposes the loan is being paid by the Generals and Northerns. In fairness and equity they should be subrogated to the rights of the Reconstruction Finance Corporation.

> "* * * the equitable doctrine of subrogation * * * has been steadily growing in importance and widening its sphere of application. It is a creation of equity and is administered in the furtherance of justice. It is applied to give the party who pays the debt the full benefit and advantage of such payment."
>
> *Rachal* v. *Smith*, 101 Fed. 159 (C. C. A. 5th).

> "The doctrine of subrogation is one of equity and not of the common law and, in its application, no attention should be paid to technicalities which are not

of an insuperable character, but broad equities should always be sought out as far as possible."

Merchants & M. Transport Co. v. *Robinson & Co.*, 191 Fed. 769-772 (C. C. A. 1st).

"These Federal cases clearly reflect the rule requiring liberal application of the doctrine of subrogation, and we think they have so far committed the Federal Courts to that rule that we ought not to refuse to follow the path they have chosen."

Burgoon v. *Lavezzo*, 92 Fed. 2nd 726-36 (C. C. A., D. C. '37).

The Series G General bonds and the 1st & Refunding bonds held by the Reconstruction Finance Corporation are to be cancelled under the Plan.

Under the Plan, the allocation of securities to the 50-Year Mortgage is based on the fact that that mortgage is now a second lien on the security on which the 1st & Refunding Mortgage is now a first lien. It makes that security and the claim that the 50-Year Mortgage will then be a first lien on the "Pieces of Lines East" the basis of allotting to the 50-Year Mortgage about $19,000,000 of Class B Contingent Interest bonds, on a parity with 20% of the General Mortgage bondholders' claim, and gives them priority over the 20% Preferred Stock allotted to the Generals.

These allotments absolutely ignore the fact that this loan is to be paid, the 1st & Refunding bonds cancelled, and these assets freed at the expense of the General Mortgage bondholders, and ignores their right to subrogation to the rights of the Reconstruction Finance Corporation.

POINT VIII

The Commission should be directed to receive evidence of facts and earnings after the date when its hearings closed in March, 1938, and to consider such evidence as well as the evidence received in the District Court.

Our argument has been based upon the record but if the Court shall take judicial notice of the changed conditions affecting the earnings of railroads generally (as it did in *Atcheson, Topeka & Santa Fe Railroad* v. *United States*, 284 U. S. 248), it will be convinced that the security for our bonds is even greater than indicated by the present record and that the approval of the present plan would be a travesty of justice.

We do not argue this point at length, believing that it will be stressed by the junior creditors and the Debtor, to all of whom it is more important than it is to us.

Conclusion

The petitioners make no attempt to controvert our claims which were asserted in the Courts below (1) that the General Mortgage is fully secured, and (2) that the securities offered us are not "of a value equal to" our claims.

Their whole argument is that the Commission, having certified that the Plan is *compatible* with the public interest, the public interest is predominant and that the Commission may take our property for the public interest without compensation.

A mortgage lien is a property right whether it be on a railroad or on a sewing machine, and the decision of this Court in *Louisville Bank* v. *Radford*, 295 U. S. 555, 602 (quoted above), applies here.

As to the applicability of the law of the land established in the *Consolidated Rock Products* case (312 U. S. 510), we cannot improve on the language of the brief of the *Reconstruction Finance Corporation*, filed in the Court below (p. 37):

> "That these principles are equally applicable in railroad reorganizations is easily established, not only by the obvious fact that the interests of the investor and the principles of value do not change with the character of the business involved, but also by the express provisions of Section 77 and by direct judicial decision."

We contend not only that the Congress did not, and did not intend to confer such power upon the Commission but that it could not have done so without violating the Fifth Amendment to the Constitution.

It would be difficult to exaggerate the importance of the questions now before the Court. Upon their decision depend not only the rights of investors—most of them fiduciaries—who have invested literally billions of dollars in these and other underlying railroad bonds, but also the credit of the Railroads of our Country.

If this Plan were approved upon this record, no sane man would ever again loan money to a railroad upon the security of its mortgage bonds.

Respectfully submitted,

FREDERICK J. MOSES,
Attorney for Trustees of Princeton University, et al., constituting the "University Group" of General Mortgage Bondholders of Chicago, Milwaukee & St. Paul Railway Company.

October 7, 1942.

I.C.C. EXHIBIT NO. 181

Witness

Committee No. 5

CHICAGO, MILWAUKEE, ST. PAUL AND PACIFIC R.R. CO

I.C.C. Finance Docket No. 10882

Allocation Made by the Debtor of the Actual System Earnings for the Year, 1936 to Mortgage Districts, in Designated Exhibits, With Various Adjustments Made by the Debtor Separately Shown, Together With Interest Requirements

	1936 System	C.T.H. & S.E. (Exh. 139-140	Milw. & Nor. (Exh. 141-142)	Chic. M. & Gary ("B" of Exh. 143, Exh. 144)	1st & Ref. Mtg. (Exh. 145-146) Lines West	Pieces of Lines East	Total	Total C.T.H.& S.E., Milw. & Nor., C.M. & G., and 1st & Ref. Mtg.	Balance Remaining for General Mtg. (Incl. Equip. Trusts
REVENUES:									
Freight	$ 91,560,382	$5,180,222	$2,656,982	$166,512	$15,839,897	$	$	$	$
Passenger	7,496,998	12,922	290,352		1,392,468				
Mail	3,077,277	9,564	129,066		326,967				
Express	1,770,062	1,392	72,579		230,246				
All Other	5,237,367	49,777	105,526	19,079	628,051				
Total Commercial Revenues	109,142,086	5,253,877	3,254,505	185,591	18,417,629	4,596,200	23,013,829	31,707,802	77,434,284
EXPENSES:									
Maint. of Way & Structures	18,561,825	980,023	380,271	74,858	4,446,537				
Maint. of Equip.	19,652,864	817,852	480,266	24,200	3,678,711				
Traffic	2,559,788	52,017	70,756	8,000	386,449				
Transportation	40,501,964	1,292,067	1,063,880	133,245	7,056,102				
General & Misc.	4,316,455	86,717	94,211	12,900	914,545				
Transportation for Investment—Cr.	Cr. 348,542	Cr. 4,040			Cr. 135,368				
Total Operating Expenses	85,244,354	3,224,636	2,089,384	253,203	16,346,976	3,139,400	19,486,376	25,053,599	60,190,755
Net Rev. from Ry. Oper.	23,897,732	2,029,241	1,165,121	def. 67,612	2,070,653	1,456,800	3,527,453	6,654,203	17,243,529
TAXES:									
Ordinary Taxes	6,253,943	222,346	139,667		1,641,012	233,100	1,874,112		
R.R. Retirement Taxes	1,523,755	52,290	37,332		299,128	56,100	355,228		
Social Security Taxes	357,302	14,706	10,417		75,762	19,000	94,762		
Total Taxes	8,135,000	289,342	187,416	54,900	2,015,902	308,200	2,324,102	2,855,760	5,279,240
Ry. Oper. Income	15,762,732	1,739,899	977,705	def. 122,512	54,751	1,148,600	1,203,351	3,798,443	11,964,289
Equipment Rents—Dr.	3,334,094	846,480	218,523	20,500	590,264				
Joint Facility Rents—Dr.	2,967,280	112,261	2,886	21,360	371,554				
Total Rents—Dr.	6,301,374	958,741	221,409	41,660	961,818	841,900	1,803,718	3,025,728	3,275,646
Net Ry. Operating Income	9,461,358	781,158	756,296	def. 164,372	def. 907,067	306,700	def. 600,367	772,715	8,688,643
Other Income (Net):									
Other Income $1,459,580							(402,031(e)		
Miscellaneous Deductions 69,607	1,389,973	Dr. 38	3,342	3,005	8,699	13,500	(22,199	430,539	959,434
Income Available for Fixed Charges	10,851,331	781,120	759,638	def. 161,367	def. 898,368	320,200	def. 176,137	1,203,254	9,648,077
Less: Certain Fixed Charges Other than Interest on Funded Debt Deducted from Mortgage Line Earnings but Not Deducted from System Earnings; (Exh. No. —)	181,335								181,335
Total Income Available for Interest Before Debtor's Adjustments	10,669,996	781,120	759,638	def. 161,367	def. 898,368	320,200	def. 176,137	1,203,254	9,466,742
DEBTOR'S ADJUSTMENTS:									
Revenue from Haul of Company Material		Cr. 2,209,006(a)	Cr. 13,051(b)	Cr. 94,395(b)	Cr. 663,879(b)		Cr. 663,879(b)	Cr. 2,980,331	Dr. 2,980,331
Charge for Hauling Company Material—Cost Basis			Dr. 52,806	Dr. 2,382	Dr. 67,533	Dr. 135,100	Dr. 202,633	Dr. 257,821	Cr. 257,821
Rent for Use of System Equipment		(Incl. Above)	Dr. 146,944	(Incl. Above)	Dr. 806,513	(Incl. Above)	Dr. 806,513	Dr. 953,457	Cr. 953,457
Rent for Use of Joint Facilities			Cr. 15,000			Dr. 15,000	Dr. 15,000		
Switching Expense at Milwaukee			Dr. 92,757	Cr. 23,538				Dr. 92,757	Cr. 92,757
Charge for Handling Empties								Cr. 23,538	Dr. 23,538
Total Adjustments (As Per Exhibits)	—	Cr. 2,209,006	Dr. 264,456	Cr. 115,551	Dr. 210,167	Dr. 150,100	Dr. 360,267	Cr. 1,699,834	Dr. 1,699,834
Total Income Available (As Per Exhibits)	10,669,996	2,990,126	495,182	def. 45,816	def. 1,108,535 (e)	170,100 (e)	def. 536,404	2,903,088	7,766,908
Adjustment to put Revenues, Expenses and Equipment Rents on a Cost of Service Basis (Exh. No. —)		Dr. 949,939						Dr. 949,939	Cr. 949,939
Total Income Available, as Adjusted by Debtor	10,669,996	2,040,187	495,182	def. 45,816			def. 536,404	1,953,149	8,716,847
		65,530							1,155,159

	1936 System	C.T.H. & S.E. (Exh. 139-140	Milw. & Nor. (Exh. 141-142)	Chic. M. & Gary ("B" of Exh. 143, Exh. 144)	1st & Ref. Mtg. (Exh. 145-146) Lines West	Pieces of Lines East	Total	C.T.H.& S.E., Milw. & Nor., C.M. & G., and 1st & Ref. Mtg.	Remaining for General Mtg. (Incl. Equip. Trusts
REVENUES:									
Freight	$ 91,560,382	$5,180,222	$2,656,982	$166,512	$15,839,897	$	$	$	$
Passenger	7,496,998	12,922	290,352		1,392,468				
Mail	3,077,277	9,564	129,066		326,967				
Express	1,770,062	1,392	72,579		230,246				
All Other	5,237,367	49,777	105,526	19,079	628,051				
Total Commercial Revenues	109,142,086	5,253,877	3,254,505	185,591	18,417,629	4,596,200	23,013,829	31,707,802	77,434,284
EXPENSES:									
Maint. of Way & Structures	18,501,825	980,023	380,271	74,858	4,446,537				
Maint. of Equip.	19,652,864	817,852	480,266	24,200	3,678,711				
Traffic	2,559,788	52,017	70,756	8,000	386,449				
Transportation	40,501,964	1,292,067	1,063,880	133,245	7,056,102				
General & Misc.	4,316,455	86,717	94,211	12,900	914,545				
Transportation for Investment—Cr.	Cr. 348,542	Cr. 4,040			Cr. 135,368				
Total Operating Expenses	85,244,354	3,224,636	2,089,384	253,203	16,346,976	3,139,400	19,486,376	25,053,599	60,190,755
Net Rev. from Ry. Oper.	23,897,732	2,029,241	1,165,121	def. 67,612	2,070,653	1,456,800	3,527,453	6,654,203	17,243,529
TAXES:									
Ordinary Taxes	6,253,943	222,346	139,667		1,641,012	233,100	1,874,112		
R.R. Retirement Taxes	1,523,755	52,290	37,332		299,128	56,100	355,228		
Social Security Taxes	357,302	14,706	10,417		75,762	19,000	94,762		
Total Taxes	8,135,000	289,342	187,416	54,900	2,015,902	308,200	2,324,102	2,855,760	5,279,240
Ry. Oper. Income	15,762,732	1,739,899	977,705	def. 122,512	54,751	1,148,600	1,203,351	3,798,443	11,964,289
Equipment Rents—Dr.	3,334,094	846,480	218,523	20,500	590,264				
Joint Facility Rents—Dr.	2,967,280	112,261	2,886	21,360	371,554				
Total Rents—Dr.	6,301,374	958,741	221,409	41,660	961,818	841,900	1,803,718	3,025,728	3,275,646
Net Ry. Operating Income	9,461,358	781,158	756,296	def. 164,372	def. 907,067	306,700	def. 600,367	772,715	8,688,643
Other Income (Net):									
Other Income $1,459,580							(402,031(e)		
Miscellaneous Deductions 69,607	1,389,973	Dr. 38	3,342	3,005	8,699	13,500	(22,199	430,539	959,434
Income Available for Fixed Charges	10,851,331	781,120	759,638	def. 161,367	def. 898,368	320,200	def. 176,137	1,203,254	9,648,077
Less: Certain Fixed Charges Other than Interest on Funded Debt Deducted from Mortgage Line Earnings but Not Deducted from System Earnings; (Exh. No. —)	181,335								181,335
Total Income Available for Interest Before Debtor's Adjustments	10,669,996	781,120	759,638	def. 161,367	def. 898,368	320,200	def. 176,137	1,203,254	9,466,742
DEBTOR'S ADJUSTMENTS:									
Revenue from Haul of Company Material		Cr. 2,209,006(a)	Cr. 13,051(b)	Cr. 94,395(b)	Cr. 663,879(b)		Cr. 663,879(b)	Cr. 2,980,331	Dr. 2,980,331
Charge for Hauling Company Material—Cost Basis			Dr. 52,806	Dr. 2,382	Dr. 67,533	Dr. 135,100	Dr. 202,633	Dr. 257,821	Cr. 257,821
Rent for Use of System Equipment		(Incl. Above)	Dr. 146,944	(Incl. Above)	Dr. 806,513	(Incl. Above)	Dr. 806,513	Dr. 953,457	Cr. 953,457
Rent for Use of Joint Facilities			Cr. 15,000			Dr. 15,000	Dr. 15,000		
Switching Expense at Milwaukee			Dr. 92,757	Cr. 23,538				Dr. 92,757	Cr. 92,757
Charge for Handling Empties								Cr. 23,538	Dr. 23,538
Total Adjustments (As Per Exhibits)		Cr. 2,209,006	Dr. 264,456	Cr. 115,551	Dr. 210,167	Dr. 150,100	Dr. 360,267	Cr. 1,699,834	Dr. 1,699,834
Total Income Available (As Per Exhibits)	10,669,996	2,990,126	495,182	def. 45,816	def. 1,108,535 (e)	170,100 (e)	def. 536,404	2,903,088	7,766,908
Adjustment to put Revenues, Expenses and Equipment Rents on a Cost of Service Basis (Exh. No. —)		Dr. 949,939						Dr. 949,939	Cr. 949,939
Total Income Available, as Adjusted by Debtor	10,669,996	2,040,187	495,182	def. 45,816			def. 536,404	1,953,149	8,716,847
Interest on Equip. Trusts		65,530 (Ser. E)							1,155,159
Balance		1,974,657	495,182	def. 45,816			def. 536,404		7,561,688
Interest on Mtg. Bonds (Incl. Pledged Bonds)		1,099,330(c)	323,505	150,000		(Pledged)	535,380		6,512,855(d)
Balance		875,327	171,677	def. 195,816			def. 1,071,784		1,048,833
Times Interest on Mtg. Bonds Earned		1.80	1.53						1.16

Notes:
(a) At tariff rates.
(b) On costs basis.
(c) Includes $75,750 on C.T.H. & S.E. 1st & Ref. Bonds pledged under 1st & Ref. Mortgage.
Mortgage.
(d) Includes $560,600 on General Mortgage 5s pledged.
(e) Interest and dividends on pledged securities not assigned to lines East or West.

Dated Jan. 27, 1938.